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### Deposited in DRO:

21 December 2013

### Version of attached file:

Presentation

### Peer-review status of attached file:

Peer-reviewed

### Citation for published item:

Chirita, Anca D. (2013) 'The impact of the European Union current crisis on law, policy and society.', Centre for European Legal Studies (CELS) Seminar University of Cambridge, 16 October 2013.

### Further information on publisher's website:

<http://www.cels.law.cam.ac.uk/press/events/2013/10/cels-lunchtime-seminar-impact-european-union-current-crisis-law-policy-and>

### Publisher's copyright statement:

### Additional information:

Draft article to be published in the Cambridge Yearbook of European Legal Studies, Vol. 16, 2013-2014 published by Hart Publishing

<http://www.hartpub.co.uk/SeriesDetails.aspx?SeriesName=Cambridge+Yearbook+of+European+Legal+Studies>

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## THE IMPACT OF THE EUROPEAN UNION CURRENT CRISIS ON LAW, POLICY AND SOCIETY\*

CELS Seminar, Cambridge, October 16, 2013

**Abstract:** *The purpose and methodology of this article is as follows: first, to understand the general nature of the current crisis (banking, financial, debt, currency, constitutional, political) from a socio-legal, economic, ideological and political perspective; then, to analyse the complexity of the multiple causes which have led to the current crisis in particular areas of law (financial, banking, securities, contract, competition and corporate law) in which it has manifested itself and the sectors of the economy it has affected; and, finally, to criticise law in action and the management of the crisis through political decision-making (state intrusiveness), that is, the various responses and reactions to the crisis and the effectiveness of the measures implemented by policy-makers and enforcers, and, inter alia, to question the constitutional legitimacy of the TBTF (Too-Big-to-Fail) theory as a predominant doctrine and criterion of state intervention in the economy.*

*A multi-layered level of economic, social, and political governance is envisaged through insights from microeconomics, by looking at how economic agents have affected individuals such as consumers; from macroeconomics, by looking at how state intervention in the economy has impacted upon taxpayers and the human and social costs of the crisis; and from political economy by looking through the lenses of ideology and policy and reflecting on the role of neoliberalism today.*

*To conclude, the heavy reliance on the TBTF doctrine became a European 'Too Big to Crash' test which signals past memories and fears of an eventual repeat of the 1929 Wall Street crash, which to date has been avoided by all possible methods of political intervention. Unfortunately, competition law could be seen as the scapegoat of this unprecedented restructuring of the banking and financial markets through competition policy's illegitimate and undeserved but generous state aid to benefit mostly inefficient and unscrupulous financial game players. This last recognition leads us to question the adequate measures of profit-seeking capitalism.*

### I. ON THE NATURE AND HISTORY OF THE CRISIS

The nature of the current crisis has been determined by the sectors of the economy which are most affected by economic failures. On the basis of this starting criterion, large financial institutions, such as commercial, investment or securities banks and other major corporations, involved in financial service transactions have experienced a large number of defaults; this has been recognised as a *banking* crisis.<sup>1</sup> However, a greater risk to affect and spread the banking crisis to other financial institutions has made it *systemic*. Before the crisis, banks experienced longer periods of credit expansion, which had also led to a rise of asset prices (real estate, equity), above the level of economic growth, namely, the gross domestic product (GDP). On the negative side, the credit boom reached a peak and burst into a price 'bubble', i.e. house prices fell below outstanding balances on home mortgages. Thus, a *sovereign* debt crisis then emerged as defaults on payments of debt obligations became the rule which called for the restructuring of the banking sector. This process meant offering debtors less favourable terms than the expected capital gains.

The global crisis emerged first in the US subprime market,<sup>2</sup> which generated losses during summer 2007 to mid-2008. Hundreds of billions of dollars in bad mortgage loans initially set at bargain rates<sup>3</sup> were then reset at market rates so that when housing prices started to fall, owners defaulted on their payments. This was followed by the

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<sup>1</sup> CM Reinhart and KS Rogoff, *This Time is Different: Eight Centuries of Financial Folly* (Princeton University Press, 2009); J de Haan, S Oosterloo and D Schoenmaker, *Financial Markets and Institutions: A European Perspective* (2<sup>nd</sup> ed, Cambridge, CUP, 2012); S Valdez and P Molyneux, *An Introduction to Global Financial Markets* (7th ed, Palgrave Macmillan, 2013). Economists predict an economic downturn where output falls by 9% over two years; unemployment rises up to 7% over 4 years; and government debt increase by 86% over the next 3 years following a systemic banking crisis.

<sup>2</sup> See M Jarsulic, 'The Origins of the US Financial Crisis of 2007: How a House-Price Bubble, a Credit Bubble, and Regulatory Failure Caused the Greatest Economic Disaster since the Great Depression' in MH Wolfson and GA Epstein (eds) *The Handbook of the Political Economy of Financial Crisis* (Oxford, OUP, 2013) 30.

<sup>3</sup> Interest rates were very low due to large capital flows from abroad to the US economy, the Federal Reserve, and low inflation.

bailout of Bear Stearns, the US's fifth largest investment bank; the nationalisation of mortgage agencies, Fannie Mae and Freddie Mac; and Lehman Brothers' bankruptcy in September 2008. Until late October of that year, a global loss of confidence created a systemic risk of collapse. The recession manifested itself through sharp increases in budget deficits and slow economic recovery. In addition, tax revenues plummeted and the limits of the Stability and Growth Pact of 1997<sup>4</sup> were breached. After September 2008, European Union (EU) rescue policies focused on restoring the liquidity of banks and guarantees, while the ECB (European Central Bank) and national central banks, outside the euro, adjusted the provision of liquidity and cut interest rates.<sup>5</sup> The European Recovery Plan provided a discretionary fiscal stimulus of €200 bn, of which €170 bn was used for budgetary expansion and the rest to 'boost demand and stimulate confidence'.<sup>6</sup> A European Financial Stabilisation Mechanism provided Member States with another €500 billion. Until March 2009, investors' focus was on the global economic downturn. Not until mid-March 2009, were there any signs of stabilisation.<sup>7</sup>

Unique due to its geo-political architecture, the European crisis revealed that it is not solely economic actors who can default on their contractual obligations; Member States, such as Greece, can also fail to keep up with their borrowing costs. Furthermore, political pursuits of monetary union and its single currency highlight its complexity, as pictured above at the *micro*-economic level. At the *macro*-economic level, states which maintain fixed exchange rates may also experience a *currency* crisis where the value of the national currency falls suddenly as a result of a loss of confidence followed by speculative attacks.<sup>8</sup> When the ECB launched the single currency, only 12 Member States joined the Eurozone, followed five years later by another five Member States.<sup>9</sup>

The Greek tragedy has led the EU to reconsider both the political and the constitutional dimension of the *sovereign debts* crisis. In May 2010, the Union set a precedent by granting a total of €80 bn to Greece.<sup>10</sup> In this context, the solidarity with a Member State's economic failure triggered a political crisis fuelled with heated legal arguments. In particular, solidarity is pre-empted by Article 125 (1) TFEU itself, which rules out state bailouts<sup>11</sup> when it says that both the Union and its Member States *shall* not be liable for or assume commitments of central governments.<sup>12</sup> It became known that Greece had manipulated its data for accession to the single currency,<sup>13</sup> which then called for an evaluation of its debts and rescue package. A *constitutional* crisis emerged which suggested Greece's possible exit from the Eurozone. The precarious situation of sovereign debts transformed this crisis into a Euro currency crisis amid speculations over Greece's economy. This has been the first major test of both economic and, foremost, social European integration, which has revealed the perils of free capital markets, liberalisation, and a single currency based on institutional foundations which were not capable of sharing the economic costs of major economic imbalances. For instance, in May 2011, Portugal received a €78 bn rescue package from the EU and the IMF.<sup>14</sup>

In the absence of a fiscal union, the Founding Treaties proposed an Economic and Monetary Union (EMU) subject to strict convergence criteria. Thus, the crisis has highlighted the existing economic disparities in terms of economic development across the EU. Being part of a 'Union of benefits' has made Member States economically and socially responsible for another Member State's inefficiency; in the same way, the financialization of capital services worldwide has triggered the responsibility of various economic actors, states, institutions, and the wider society. It

<sup>4</sup> See R Guttman and D Plihon, 'Whither the Euro? History and Crisis of Europe's Single-Currency Project' in *Handbook* (2013) 368. The SGP imposed uniform limits for budget deficits and public-debt level.

<sup>5</sup> C Quigley, 'Review of the Temporary State Aid Rules Adopted in the Context of the Financial and Economic Crisis' 3 J of Comp Law & Practice 3 (2012) 237. On state aid generally see C Quigley and AM Collins, *EC State Aid Law and Policy* (Oxford, Hart Publ, 2003).

<sup>6</sup> Ibid.

<sup>7</sup> Positive signs are noted in 'Towards a Genuine Economic and Monetary Union', available at [http://www.consilium.europa.eu/uedocs/cms\\_data/docs/pressdata/en/ec/134069.pdf](http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/134069.pdf).

<sup>8</sup> For example, in 1999, several EU Member States attempted to stabilise their exchange rates through the Exchange Rate Mechanism.

<sup>9</sup> See P Arestis and M Sawyer, 'Can the Euro Survive after the European Crisis?' in *The Euro Crisis* Arestis and Sawyer (Eds) Palgrave Macmillan 2012. In 1999, Denmark, Sweden and the UK decided to remain outside the Eurozone.

<sup>10</sup> E Chiti and PG Teixeira, 'The Constitutional Implications of the European Responses to the Financial and Public Debt Crisis' 50 CMLR (2013) 686; Guttman and Plihon, 372 mention a total of €750 bn, including the IMF granted to Greece.

<sup>11</sup> M Ruffert, 'The European Debt Crisis and European Union Law' 48 CMLR (2011) 1785.

<sup>12</sup> The only exception in Art 125 (1) is 'without prejudice to mutual financial guarantees for the joint execution of a specific project'.

<sup>13</sup> See e.g. <http://euobserver.com/economic/28871>.

<sup>14</sup> Guttman and Plihon 372.

has raised the question of who is primarily responsible for the crisis. This is not easy to answer either before or after judging the roots of the crisis.

## II. ON THE ROOTS OF THE CRISIS: WHAT WENT WRONG?

The literature on the economic crisis abounds in suggestions of what went wrong before and after the crisis. Thus failures appear first as poor economic governance because the State employs ineffective means of correlating and/or, whenever possible, correcting macroeconomic indicators which later affect individual decision-making. For example, some of the convergence criteria which Member States are required to fulfil prior to joining the Eurozone emerge first as economic indicators which went wrong, such as public deficit and spending, growth rate, GDP, or interest rates. Valdez and Molyneux<sup>15</sup> have identified the following major macroeconomic imbalances: (i) large and persistent current account *deficits* following previous surpluses due to capital flows from emerging to rich industrial economies; (ii) a long period of low real *interest rates* fuelled by deflationary concerns; (iii) a *credit boom* for home mortgage lending which put up the housing prices before the crisis by more than 30%;<sup>16</sup> (iv) low interest rates that encouraged *consumer spending* and persuaded banks to take on more *risk* in various long-term contracts.

Among the leading variables indicating a *financial crisis* are rising defaults and government deficits, the rapid growth of credit and money supply, rising real interest rates, declining GDP etc.<sup>17</sup>

This simplified picture has to be explored in greater depth to identify what went wrong with private and public actors, the state, law in action, policy makers, and policy influencers.<sup>18</sup>

(A) *What went wrong with the state?* The state gave access to easy credit (making too much money available) through a lax monetary policy (lowering interest rates). It tolerated the 'shadow banking system' through the transformation of investment banks into holding companies to have access to governmental funding,<sup>19</sup> and it later bailed out banks which took risks, and therefore encouraged them to indulge in more risk-taking.

(B) *What went wrong with private economic actors?* Individual economic actors (consumers, borrowers, lenders) underestimated the economic cost and took on more risks or engaged in highly hazardous and speculative contracts (loans, partly variable mortgage rates, bond and loan insurance contracts).<sup>20</sup> In other words, consumers failed to be aware of risks to themselves (as if this were possible) and soon, complexity was mistaken for sophistication, with consumers assuming that their investments and deposits were safe. Corporate managers failed to evaluate risks before entering into complex transactions (securitization, investment vehicles, repos, credit default swaps); in sum, the collective solidarity of banks had been oriented towards hazardous or foolish risk-taking,<sup>21</sup> market indiscipline, and market abuse, irrespective of whether or not the bank itself held monopoly power. Managers increased returns by boosting excessive leverage, i.e., the return on equity as the major indicator of a firm's performance.<sup>22</sup> In essence, the ownership of capital

<sup>15</sup> Supra n 1.

<sup>16</sup> Between 2003 and 2007, source: BIS.

<sup>17</sup> See Tymoigne 102.

<sup>18</sup> See a previous classification in RM Lastra and Wood, 'The Crisis of 2007-2009: Nature, Causes, and Reactions' 13 JIEL (2010) 3, 531; 537; L Garicano and R Lastra, 'Towards a New Architecture for Financial Stability: Seven Principles' 13 JIEL (2010) 3, 597.

<sup>19</sup> E Avgouleas, 'The global financial crisis, behavioural finance and financial regulation: in search of a new orthodoxy' 9 J of Corporate L Studies 2009, 23; AM Mateus, 'Banking Regulatory Reform: 'Too Big to Fail' and What Still Needs to be Done', available on SSRN. The US abolished the Glass-Steagall Act 1933 to separate commercial from investment banking; O Kessler and B Wilhelm, 'Financialization and the Three Utopias of Shadow Banking' 17 Comp and Change 3 (2013), 251 on information asymmetries and 'moral' hazard problems; on government failure see ME Stucke, 'Lessons from the Financial Crisis' 77 Antitrust LJ, 314.

<sup>20</sup> F Möslin, 'The focus of regulatory reforms in Europe after the global financial crisis: from corporate to contract governance' in Sun, Stewart and Pollard (eds) 286.

<sup>21</sup> Banks and firms were taking on extensive risks and their solvency was threatened; managers were given incentives to take on greater risks so as to generate higher returns for shareholders. On collective moral hazard, see e.g. E Farhi and J Tirole, 'Collective Moral Hazard, Maturity Mismatch and Systemic Bailouts' Am Ec Rev 2011.

<sup>22</sup> The 2009 Report of the OECD Steering Group on Corporate Governance identified excessive remuneration, risk management, board practices and the exercise of shareholder rights as main problematic areas of corporate governance.

was financed by debts.<sup>23</sup> The net income generated to shareholders created the bonus culture, while compensation schemes encouraged short-run risk-taking.

(C) *What went wrong with policy?* Macroeconomic policy registered numerous failures through relaxed credit, but austere public spending,<sup>24</sup> followed by an industrial restructuring of banks through the application of the TBTF doctrine of state intervention in the economy. The lack of competition intervention in the banking sector, including investment, insurance, securities, and lending,<sup>25</sup> has been significant since less interventionist approaches to mergers of large banking institutions allowed them to go ahead and become TBTF and 'Too-Big-to-Supervise'.<sup>26</sup> As banks were allowed to merge, they escaped competition scrutiny<sup>27</sup> and were encouraged to compete, which exacerbated risk-taking through the relaxed risk assessment and improper disclosure requirements put in place to uncover banks' speculative pursuits.<sup>28</sup> In 2012, the European Commission finally activated its competition policy, which helped to block a mega-merger between Deutsche Börse and the New York Stock Exchange<sup>29</sup> in the market for financial derivatives.

Many believed that the unaccomplished economic, monetary, and fiscal integration of Member States was another culprit, as was the absence of a central authority<sup>30</sup> to deal with the crisis.

(D) *What went wrong with law in action?* There was a lack of or inadequate regulation of special contracts in the banking, financial and securities sector, in particular, the excessive use of securitization as a financial innovation to engineer debts 'cleansing'; excessive sophistication of commercial contracts<sup>31</sup> in finance and securities; and banking without codes of honest business practices or models of contracts in place for both consumers and businesses, in particular, for derivatives trading.<sup>32</sup> As investment and commercial banks became increasingly sophisticated, they created innovative products which were not priced accurately. It was impossible to assess the moral hazard, i.e., risk measurement, due to innovative securitized products.<sup>33</sup> The use of 'soft' law<sup>34</sup> is yet another undemocratic means by which state aid policy has turned current competition law into a major restructuring of the banking industry.

(E) *What went wrong with European institutions?* As regards institutional responses to the crisis, it took until 12 November 2008 for the Commission to propose tighter rules for credit rating agencies; until 29 April 2009 to present a draft directive on hedge funds, private equity and other alternative investment funds;<sup>35</sup> until 23 September 2009 to propose a detailed legislative package for financial supervision<sup>36</sup> (a European Systemic Risk Board for macro-prudential supervision and a micro-prudential supervision

<sup>23</sup> Profits had to be paid to bond holders and other creditors plus a competitive return to equity owners; see Kregel, 237.

<sup>24</sup> MH Böheim, 'Competition policy: ten lessons learnt from the financial crisis' 38 *Empirica* (2011) 315.

<sup>25</sup> See for the US JW Markham, 'Lessons for Competition Law from the Economic Crisis: The Prospect for Antitrust Responses to the 'Too-Big-to-Fail' Phenomenon', XVI *Fordham J of Corporate & Financial Law*, 263.

<sup>26</sup> Stucke, 319; on rising bank concentration see FM Scherer, 'Financial Mergers and their Consequences' Harvard Kennedy School of Government Research Working Paper 19 (2013).

<sup>27</sup> See D Zimmer and L Rengier, 'Entflechtung, Fusionskontrolle oder Sonderregulierung für systemrelevante Banken? Ansätze zur Lösung des 'Too-big-to-fail' Problems' 8 *Zeitschrift für Wettbewerbsrecht* (2010) 105, who proposed a specific merger control, including a 'decartelization' of banks.

<sup>28</sup> Vives, 487.

<sup>29</sup> Case COMP/M6166 *Deutsche Börse/NYSE Euronext* OJ C 199/2011.

<sup>30</sup> The International Monetary Fund 2011.

<sup>31</sup> L Buchheit, 'We Made it Too Complicated' 27 *Int Financial L Rev* (2008) 24 'When history looks back on this crisis, a big culprit will be the astonishing complexity of modern financial instruments and the drafting of their contracts'.

<sup>32</sup> Brummer, 223.

<sup>33</sup> Innovative products were backed by assets, such as subprime mortgages (loans to high risk borrowers) with short booming span which led to an exaggeration of the low risk associated with securitized assets.

<sup>34</sup> C Brummer, 'Why Soft Law Dominates International Finance-And Not Trade' 13 *JIEL* (2010) 3, 623; retrospectively see e.g. AF Lowenfeld, 'The International Monetary System: A Look Back Over Seven Decades' 13 *JIEL* (2010) 3, 575; JP Trachtman, 'The International Law of Financial Crisis: Spillovers, Subsidiarity, Fragmentation and Cooperation' 13 *JIEL* (2010) 3, 719; G Hufbauer and DD Xie, 'Financial Stability and Monetary Policy: Need for International Surveillance' 13 *JIEL* (2010) 3, 939.

<sup>35</sup> Source: EurActiv, 'Financial Regulation: The EU's agenda', 1 April 2009 available at <http://www.euractiv.com/euro-finance-regulation-eus-agenda-links-dossier-188497>.

<sup>36</sup> Brummer, 225 is critical on the Basel Committee's 'Core Principles for Effective Banking Supervision' which foresee an eventual exit of banks that are no longer able to meet supervisory requirements but do not have any mechanism to allow their exit in practice.

comprising the European Banking Authority, the European Securities and Market Authority and the European Insurance and Occupational Pensions Authority); until October 2010 to discuss a tax on financial transactions; until March 2011 to draft new rules on mortgage lending in the EU; and until June 2011 to unveil million-euro fines for rule-breaking bankers. Apart from lax lending policies and wholesale gambling on financial markets, poor credit checks run by credit rating agencies<sup>37</sup> are other responsible factors, in particular, ratings given to securitized mortgages which undermined bank balance sheets.<sup>38</sup> Credit rating agencies have also been blamed for creating the European *sovereign* debt crisis due to major conflicts of interest and faulty business models.<sup>39</sup>

(F) *What went wrong with society?* None of the above is said to have happened without the usual suspects: greed,<sup>40</sup> euphoria etc.

(G) *What went wrong with influencers?* This refers to leading academic and economic experts who influenced policy-making and on whom policy-makers later relied to reshape economic and social governance and/or manage the crisis; in particular, there was a fervent reliance on faulty neoclassical economic theories<sup>41</sup> and liberal ideologies,<sup>42</sup> an over-reliance on mathematical risk models which failed to adequately predict and mitigate corporate risk,<sup>43</sup> and utopian interpretations from the sciences.<sup>44</sup>

(H) *A knock-on effect of the limits of knowledge?* This is attributed to the 'narrow' focus of modern antitrust law<sup>45</sup> and the lack of interdisciplinary understanding, not only of law with other sciences, such as economics or sociology,<sup>46</sup> but among competition, contract, finance, banking and corporate law,<sup>47</sup> which led Westbrook to explain:

*'Financial markets are legal. Collateral is a form of property; derivatives are contracts; corporations and fiat money are creatures of law. Economics, however, has always aspired to be a natural science, and so has considered the social as if it were natural. This fundamental ontological error has led to fanciful pricing models, as if we could model the movements of legal instruments like we model the movements of the stars.'*<sup>48</sup>

In other words, the practical inability of macroeconomics to test its predictions empirically has played a major role in the history of global crisis.<sup>49</sup> Thus, the use of tools such as statistics and the reliance on macroeconomic models by

<sup>37</sup> IOSCO's Code of Conduct for Credit Rating Agencies was revised in 2008 see IOSCO, Objectives and Principles of Securities Regulation (2010), available at <http://www.compliance-exchange.com/governance/library/ioscoprinciples2010.pdf>.

<sup>38</sup> On credit rating agencies, inadequate risk assessment models, see RM Gadbaw, 'Systemic Regulation of Global Trade and Finance: A Tale of Two Systems' 13 JIEL (2010) 3, 555. Agencies rated firms as high and investments as low risk. The increased number of credit rating agencies led to increased competition which devalued the standards of their ratings.

<sup>39</sup> Kessler and Wilhelm, 260; N Petit, 'Credit Rating Agencies, the Sovereign Debt Crisis and Competition Law' Eur Comp J (2011) 587; see Franchoo and Pollard (2012) on the statement of objections against Standard & Poor's regarding alleged unfair pricing for the use of International Securities Identification Numbers.

<sup>40</sup> G Dymksi, 'Bank Lending and the Subprime Crisis' in *Handbook* (2013) 413.

<sup>41</sup> ME Stucke, 'Teaching Antitrust After the Financial Crisis' 8 J of Business & Technology L 1 (2013), 209 with the suggestion that behavioural economics is now 'mainstream'; P Krugman (2009) argued that the reason for the weakness or deregulation of financial markets is the belief in the efficiency and self-correctness of the financial markets; J Crotty, 'The Realism of Assumptions does Matter: Why Keynes-Minsky Theory Must Replace Efficient Market Theory as the Guide to Financial Regulation Policy' in *Handbook* (2013) 134.

<sup>42</sup> See RA Posner, *A Failure of Capitalism: The Crisis of '08 and the Descent into Depression* (Cambridge, Massachusetts, Harvard Univ Press, 2009). Posner identified one of the causes of the crisis as *laissez-faire* liberalism, 235.

<sup>43</sup> F Akinbami, 'Is meta-regulation all it's cracked up to be? The case of UK financial regulation' 14 J of Banking Regulation 1 (2013) 20.

<sup>44</sup> Utopian interpretations of economic theories such as the trust in the superiority of mathematics, game theory and modelling over rigorous disciplines such as law, political science, psychology, sociology and history.

<sup>45</sup> Markham, 265. As Pitofsky put it: 'It is bad history, bad policy and bad law to exclude certain political values in interpreting antitrust law'.

<sup>46</sup> See the insightful contributions of I Lianos, 'Judging' Economists: Economic Expertise in Competition Law Litigation: A European View' in I Kokkoris and I Lianos (eds) *The Reform of EC Competition Law: New Challenges* (Kluwer Law Int, 2010) 185; I Lianos and C Genakos, 'Econometric Evidence in EU Competition Law: An Empirical and Theoretical Analysis' CLES Research Paper 06/2012.

<sup>47</sup> T Cottier, 'Challenges Ahead in International Economic Law' 12 JIEC 3 (2009) 12: The financial crisis 'epitomizes the failures of a strictly disciplinary tradition of fragmentation and specialization, and the lack of truly interdisciplinary research'.

<sup>48</sup> D Westbrook, *Out of Crisis: Rethinking our Financial Markets* (Boulder, Paradigm Publ., 2009).

<sup>49</sup> G Kirchgässner, 'Die Krise der Wirtschaft: Auch eine Krise der Wirtschaftswissenschaften?' 10 *Perspektiven der Wirtschaftspolitik* 4 (2009) 447, 452: 'Dies ist ein Preis, den wir dafür zahlen müssen, dass wir zumindest im Bereich der Makroökonomik –keine experimentelle Wissenschaft sind: makroökonomische Experimente sind nie kontrolliert und sollten auch sehr zurückhaltend eingesetzt werden, da sie dann, wenn sie schief



central banks has proven to be useful. In particular, micro econometrics has demonstrated how a series of macroeconomic measures, specifically those targeting active employment policies, impact upon individuals. Nevertheless, these tools remain limited and have proven to be grossly inadequate or even counterproductive in practice.<sup>50</sup>

One can infer from the above that it is not enough to have identified the real cause or the plethora of causes which have contributed to this crisis if the means of correcting the resulting negative effects have not been fully or properly implemented. Depending on how we ought to rank them, a preliminary balance of responsibility for wrongdoing sees institutional problems of leading authorities which ought to have prevented and managed the crisis (governments, regulators), legal problems regarding the economics of special contracts which imply a higher 'moral' risk, non-interventionist competition supervision at a microeconomic level, inadequate supervision of 'shadow banking',<sup>51</sup> and the influence of schools of economics/economists on crisis management. Given the complexity of this crisis, it is difficult to identify *one* major root of the crisis; rather, multiple causes have led to major negative events. In the end, there are too many wrongs but no 'rights'. It is also possible that certain causes are the effect and vice versa. Therefore, the first scenario at a microeconomic level starts with what has happened in the subprime mortgage lending market and then goes on to question the perceived influence of certain schools of economics/economists to verify their plausibility if applied to the current crisis. The problem-question builds upon these previous insights into the roots of the crisis.

### III. ON THE INTERPLAY OF MICRO- WITH MACROECONOMICS IN THE SUBPRIME<sup>52</sup> MORTGAGE LENDING MARKET

**PROBLEM-QUESTION:** *Is there a 'behavioural' or a 'state' exploitation of consumers by bankers or states respectively (low rate stimulus)?*

At a microeconomic level, consumers borrowed more on terms which were favourable in the short term, but the long-term effect was building up a bubble due to a lack of economic foresight and human irrationality (a variable interest rate inducement coupled with myopia over any eventual job loss), in other words, an unconscionable, moral hazard. It is believed that banks intentionally exploited consumers by taking advantage of their well-known decision-making biases,<sup>53</sup> namely, consumers' tendency to ignore the long-term costs of complex transactions (i.e., hiding the real costs) and so opting for an adjustable/variable interest rate, or consumers' limited experience with transactions in the market.<sup>54</sup> The relevance of antitrust laws here is the potential to find the behavioural exploitation of consumers as a form of deceptive/fraudulent conduct, such as a lender's omission of terms and conditions. It is a well-established principle that offering incomplete information to consumers about the costs of their transaction, through false statements or omissions, will give rise to contractual misrepresentation, which, in turn, if it is based on intentional behaviour, becomes fraudulent.<sup>55</sup>

Unfortunately, the existing consumer protection and available remedies have not been adequate tools for antitrust intervention due to an artificial separation of the consumer from antitrust/competition laws.<sup>56</sup> The drawback is therefore deferring behavioural economics to consumer protection laws which address information asymmetries for

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gehen, enorme gesellschaftliche Kosten haben können'. Thus one can disagree with the last paragraph since macroeconomic policies have always been *tested* on mankind and citizens have paid the social and economic costs of policy failure.

<sup>50</sup> Ibid.

<sup>51</sup> N Roubini mentioned as part of the shadow banking: broker-dealers, hedge funds, private equity groups, structured investment vehicles, money market funds, and non-bank mortgage lenders.

<sup>52</sup> Posner suggested 'subprime' as a euphemism for mortgage loans to people at high risk of default, 23.

<sup>53</sup> See also F Akinbami, 'Retail Products and the Global Financial Crisis', available on SSRN.

<sup>54</sup> M Huffman and D Heidtke, 'Behavioural Exploitation Antitrust in Consumer Subprime Mortgage Lending', available on SSRN.

<sup>55</sup> For a disposition to fraud, see MR Darby and E Karni, 'Free competition and the optimal amount of fraud' 16 J of Law and Ec 1973, 67; F Akinbami, 'Financial services and consumer protection after the crisis' 29 Int J of Bank Marketing 2 (2011) 137.

<sup>56</sup> See NW Averitt & R Lande, 'Using the 'Consumer Choice' Approach to Antitrust Law' 74 Antitrust LJ 175 (2007); A Albors-Llorens, 'Converging Models of Federalisation: Competition and Consumer Law in the EU'.

consumers who, as borrowers, are being misled through lenders' business marketing strategies. Reliable credit information is believed to correct information asymmetries<sup>57</sup> through an effective credit reporting mechanism. Recently, the hypothesis that lenders are more likely to share credit information when entry barriers are high and the threat of competition is low has been rejected empirically due to burdensome administrative costs.<sup>58</sup> Banks with larger market shares earn higher monopoly rents on their borrower information than do banks with a smaller market share. Furthermore, higher entry barriers are associated with lower transparency in credit reporting.<sup>59</sup>

Regarding the above as being true at the microeconomic level, at a macroeconomic level, Hayek's theory of trade cycle is worth highlighting as it seems far more influential in present times than it ought to be. Hayek argued that interest rates below the 'natural' rate lead banks to expand their lending in a manner which is unsustainable.<sup>60</sup> This, in turn, leads inevitably to a crisis, since businesses are misled to believe that more resources are available than is really the case.<sup>61</sup> According to his theory, it is then government action or misinformation by the central bank which 'awakes' the crisis through the banking system. In essence, however, the reaction to such governmental stimulus was an impulsive entrepreneurial spirit towards excessive lending with the above dramatic effects on the real economy. Banks were actually attracted to subprime mortgage lending by higher interest rates of 2% above fixed prime lending.<sup>62</sup> For consumers, mortgage financing became attractive; for example, a buyer could pay £350,000 with a 90% mortgage, and three years later, the house price had increased to £500,000.

According to Austrian economics, the role of the central bank is to maintain price stability so that the money supply corresponds to the real GDP. At a European level, price stability has also been firmly grounded in the 'convergence' criteria prescribed by the EU Treaty, which will be discussed in detail shortly. However, the recession predicted by Hayek was followed by the Great Depression in 1929 despite successful price stability. Hayek believed that the 1927 US Federal Reserve's intervention in the economy had only delayed, but not fixed the crisis.

Would it not be sublime to trust Hayek again, and then blame the state for the low interest rates which triggered the housing boom, and the 'Ricardo effect' for the bubble created thereafter? A serious analysis of the *cause-effect-result* phenomenon shows that but for the low interest rates, consumers would not have mortgaged, bankers would not have assumed risky lending, and everybody would have been happy. The shortcoming of the cause-effect platitude is that it is precisely the inherent risk and its hazardous multiplication that is the real cause which has resulted in the *default bubble*. However, since the maintenance of a *low* interest rate is a macroeconomic state policy, one could argue that it was the widespread reliance on this policy which created this mess. The interest-rate-effect in macroeconomics postulates that a rising price level pushes up the interest rate, which in turn, lowers consumption and new investments in plant and equipment.<sup>63</sup>

However, it would be naive to assume that a mortgage multiplier could eventually create a crisis of such proportions. There are other trading exchanges, such as credit default swaps, which operated much in the same way or even worse. In contrast, others have argued that under the influence of neoliberalism, the economy 'benefited' from an explosion of public and private credit.<sup>64</sup>

Another belief is that a recession is able to destructively correct the errors of a boom. In other words, bad businesses will collapse, which explains, partially, the rescue mechanisms put in place by the Commission. In contrast to the previous credit boom period, interest rates have to be higher to collect through deposit savings the monies needed for the liquidity of banks which are 'due' to collapse. This view has been contradicted more recently, because

<sup>57</sup> A Padilla and M Pagano, 'Sharing default information as a borrower discipline device' *European Economic Rev* (1951).

<sup>58</sup> M Bruhn, S Farazi and M Kanz, 'Bank Competition, Concentration, and Credit Reporting', The World Bank Development Research Group, Finance and Private Sector Development Team, Policy Research Working Paper 64422/2013, 5.

<sup>59</sup> *Ibid*, 16.

<sup>60</sup> FA Hayek, *Prices and Production* (London, Routledge, 1931).

<sup>61</sup> RCB Miller, 'The Austrians and the Crisis' *Economic Affairs* (Blackwell Publ, Oxford, 2009) 28.

<sup>62</sup> Research has also found a link between the use of aggressive mortgage lending and house price volatility, see A Pavlov and S Wachter, 'Subprime Lending and House Price Volatility' Univ of Pennsylvania Institute for Law and Economics, Research Paper no 08/33 (2008).

<sup>63</sup> Slavin 257.

<sup>64</sup> O'Connor 704.



‘the liquidity problems were not created by bank runs initiated by depositors, but by the unexpected decline in the value of financial assets and by the consequent reduction of interbank lending’.<sup>65</sup>

The level of interest rates is also said to depend upon the depth of the recession.<sup>66</sup> Anecdotal evidence of the promised *triple-dip* recession proves how interest rates for savings have also not been tripled, much to our own economic loss and consternation. In contrast, states were able to borrow at historically low interest rates.<sup>67</sup> Following the Austrian economics’ advice, the State has failed to raise interest rates significantly.<sup>68</sup> Rather, it has simulated a destructive recession and has practically restructured banks through recapitalisation, the difference this time being that the resources which allowed this to happen have flown directly and freely from European taxpayers (instead of crediting their saving accounts) to hazardous risk-takers. Nevertheless, irrespective of whether the process of restructuring itself should not have been implemented effectively, the real worry turns on to whether this sacrifice is actually worth anything?

Furthermore, the reverse of not encouraging government spending for fear of any taxation mismatch or of a pervasive inflationist course seems equally odd as it results in austerity, which promotes job cuts and raises unemployment levels. Whether we like it or not, the European austerity obsession has delivered economic failure, social poverty, migration and unprecedented levels of unemployment, which will be documented in this paper. Now, to return to Hayek’s prescription of ‘flexible’ wages, i.e., cutting wages to minimise unemployment and combat inflation, the latter being currently low at 1.7%, it is worth revealing that global population<sup>69</sup> growth is more than three times higher than 1.8 bn, as it was in the 1920s. This makes one particularly circumspect of creative ideas of ‘full’ employment in real terms<sup>70</sup> as applied to a different historical level in society’s development. In the EU, the last total population revealed by Eurostat in 2012 was 503.7 million, not counting 4.2 million Croatsians. As nearly 26.2 million unemployed European citizens account for 10.8% of the active work force, it means that we have an active population of 235.8 million but only 212.22 million employed citizens. If my calculations are accurate, the EU has just 41.7% of its total population in ‘full’ employment. This dramatic unemployment situation comes just after what I would call a Failed Financialization of Big Banks, and proves that what Stiglitz has already suggested about macroeconomic multipliers is true,<sup>71</sup> namely, that assessed retrospectively, the process of European restructuring of banks, with its overly generous stimulus package, has failed to generate either jobs or any extra GDP.<sup>72</sup> The record unemployment rate in the EU does not exceed the 200 million estimate of the International Labour Organization as a global crisis unemployment figure.<sup>73</sup> However, macroeconomics suggests that only an unemployment rate of 20% triggers a depression.<sup>74</sup>

Another cause of the fragile growth lies in the more restrictive and austere macroeconomic policies that are necessary to achieve the economic and monetary union.<sup>75</sup> Nevertheless, it is clear that Austrian economics offer at least one excellent tip: if undertaken, bank recapitalisation and state control is most likely to be unsuccessful. This is true in the EU when one looks at the bleak industry predictions available so far and the high unemployment rate.

To my surprise, therefore, I find I agree with Stiglitz’s suggestion that it was the rejection of the Keynesian theory of employment,<sup>76</sup> as a promoter of rigid wages,<sup>77</sup> which formed the basis of the many post-Keynesian doctrines and

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<sup>65</sup> Heimler and Jenny 363.

<sup>66</sup> Ibid, 31.

<sup>67</sup> Grahl, 43 noting examples such as Japan (0.96%), Germany (2.40%), US (2.56%), France (2.86%), UK (3%).

<sup>68</sup> Ibid.

<sup>69</sup> Currently estimated at approximately 7 bn.

<sup>70</sup> On the rejection of ‘full’ employment see L von Mises, *Human Action* (New Haven, Yale University Press, 1949).

<sup>71</sup> J Stiglitz, ‘The global crisis, social protection and jobs’ 148 *Int Labour Rev* (2009) 1, 4.

<sup>72</sup> See e.g. J Bivens and H Shierholz, ‘The Great Recession’s Impact on Jobs, Wages, and Incomes’ in *Handbook* (2013) 61.

<sup>73</sup> Clarke, 43.

<sup>74</sup> SL Slavin, *Macroeconomics* (McGraw-Hill, Irwin, Boston, 9<sup>th</sup> ed, 2009) 218.

<sup>75</sup> See e.g. G Grahl, ‘The Subordination of European Finance’ 15 *Comp and Change* 1 (2011) 34; J Stiglitz, ‘Towards a Better Measure of Well-being’ *Financial Times*, September 13, 2009.

<sup>76</sup> See Keynes’ letter to TS Elliot in DE Moggridge (Ed) *The Collected Writings of John Maynard Keynes: Activities 1940-1946. Shaping the Post-War World: Employment and Commodities* vol 27 (London, Macmillan, 1980), 384: ‘the full employment policy by means of investment is only one particular application of an intellectual theorem. You can produce the result just as well as by consuming more or working less (...). How you mix up the three ingredients of a cure is a matter of taste and experience, i.e. of morals and knowledge.’

undermined job protection and labour rights.<sup>78</sup> Nonetheless, the greatest revelation comes with the realisation that by rejecting Keynes outright, since Article 3 (3) TEU only *aspires* ('aim') 'to achieve full employment' and leaves social policy in the invisible hands of Member States, this has been *too* Hayekian.<sup>79</sup> In macroeconomics, a 5% unemployment rate means that the economy attains full employment.<sup>80</sup> The misconception of employment theory, with a strong emphasis on its 'utopian' vision of full employment, can be justified by the distrust of wage competition, which even if it could achieve labour flexibility, does so at the expense of worsening workers' conditions. According to Keynes, lowering wages would lower workers' incomes and reduce further spending on goods.<sup>81</sup> This makes Keynesian theory socially human, thus Keynes believed that capitalism has a natural tendency to cut employment.<sup>82</sup> Keynes believed that the self-correcting mechanisms of falling interest rates, prices, and wages are insufficient to stimulate investment and consumption<sup>83</sup> as a way out of the recession.<sup>84</sup> In other words, without government intervention, the economy does not move toward full employment. Thus it can be said that the Keynesian policies implemented in the 1950s and 1960s were inappropriately addressing deflation after it had ceased to represent a major threat.<sup>85</sup> Therefore, Minsky's financial fragility theory postulated that the trade cycle reacts to endogenous shocks, such as a change in monetary policy by the central bank (e.g. increasing interest rates to slow the economy for fear of inflation, or a supra-production crisis where markets are saturated with cars, electronics etc.)<sup>86</sup> and that a deficient aggregate demand triggers a stagnant unemployment situation, which could eventually attain Keynesian full employment through monetary (e.g. government spending) and fiscal policy.<sup>87</sup>

If nothing else works, another option suggested by Austrian economics is to promote competition in currency exchange. Obviously, this did not work well for the Eurozone countries which could not devalue their national currencies.<sup>88</sup> Finally, as a last resort, tax is also viewed with much scepticism.<sup>89</sup> Though granting temporary facilities to individuals contributes to raising the level of savings deposits, which, in turn, actively stimulates consumption, if it also targets those consumer goods that are to be produced in the long run and further imports, direct tax helps all too little. Since 50% of the lower taxed goods account for only 2.8% of revenues, while the upper 5% account for 63.5%, and because the marginal consumption rate falls as earnings increase, then adjusting the private consumption deficit through direct taxation is thus possible for the category of lower income taxation. Therefore, trying to fix a crisis through taxation is nothing but a vicious circle.

These insights all reveal how unhelpful economic policies or economists' predictions<sup>90</sup> are; how the crisis has destroyed them one after another, thereby shaking our society in the search for social justice, the rule of law, and a new order; and how this crisis managed to exacerbate its social and economic costs instead of 'fixing' the economy.

#### IV. ON THE MACROECONOMICS OF THE EURO CRISIS

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<sup>77</sup> See JM Keynes, 'The General Theory of Employment' 51 Quarterly J of Ec (1937) 209; Keynes, *The General Theory of Employment, Interest and Money* (London, Macmillan, 1973), also available at [www.isn.ethz.ch](http://www.isn.ethz.ch).

<sup>78</sup> Ibid, 9.

<sup>79</sup> On the rise of neoliberalism with free market theory, monetarism, supply-side and conservative economics, renewed interest in Hayek and bias against Keynesian theory, see DM Kotz, 'Changes in the Postwar Global Economy and the Roots of the Financial Crisis' in *Handbook* (2013) 399.

<sup>80</sup> Slavin 258.

<sup>81</sup> Ibid 262.

<sup>82</sup> Kirchgässner 462.

<sup>83</sup> On government spending, Keynes said that 'quantity is more relevant than quality. Even if the government employed some people to dig holes and others to fill up those holes'; see Slavin 368.

<sup>84</sup> Slavin 268.

<sup>85</sup> E Tymoigne, 'Financial fragility' in *Handbook of Critical Issues in Finance* J Toporowski and J Michell (eds) (Cheltenham, Elgar, 2012) 100.

<sup>86</sup> Macroeconomics describes the saturation of markets through the innovation theory where economic downturn continues until a new innovation takes hold. Another endogenous theory focuses on psychological factors whereas optimism triggers investments in plants, more jobs and consumer spending.

<sup>87</sup> J Kregel, 'Hyman P. Minsky' in *Handbook* (2012) 237.

<sup>88</sup> Another suggestion has been to create a mechanism by which Member States with a current account deficit could devalue in real terms and other Member States with a surplus could revalue.

<sup>89</sup> Kirchgässner 462.

<sup>90</sup> LJ Peter, *Peter's Quotations*: 'An economist is an expert who will know tomorrow why the things he predicted yesterday didn't happen today.'

Article 119 (2) TFEU refers to a single currency, namely, the euro, monetary policy, and exchange-rate policy. Its primary objective is to maintain price stability and to support the general economic policies in the Union, in accordance with the ‘principle of an open market economy with free competition’. This principle means that at a microeconomic level, free competition will be complemented by macroeconomic policy. According to Article 119 (3), macroeconomic policy shall comply with the following guiding principles: stable prices, sound public finances and monetary conditions, and a sustainable balance of payments.

Therefore, Article 140 (1) TFEU sets out the Maastricht convergence criteria for the accession of Member States to the single currency. These nominal terms are tight. They mandate that every two years the Commission and the ECB report to the Council on the progress made by the Member States regarding the achievement of economic and monetary union, with a view of the achievement of a high degree of sustainable convergence. The criteria refer respectively to the ‘achievement, sustainability, observance and durability’ of:





- (i) a high degree of price stability by looking at the inflation rate of the three best performing Member States;<sup>91</sup>
- (ii) the sustainability of the government financial position, by looking at the public deficit;
- (iii) normal fluctuation margins provided for by the exchange-rate mechanism without devaluing against the euro;
- (iv) convergence achieved by the Member State with derogation and its participation in the exchange-rate mechanism being reflected in the long-term interest-rate levels.

The primary objective of price stability is also mentioned under Article 105 of the Protocol on the European System of Central Banks (ESCB).

In sum, the above economic criteria refer to the following nominal values: inflation (lower than 1.5%), exchange rate (+/- 15%), long-term interest rates (no more than 2% higher than the unweighted arithmetic coverage of the similar 10-year government bond yields in the 3 Member States with the lowest HICP inflation), budget deficit (lower than 3% GDP) and a government public debt criterion (lower than 60%). These criteria aim to establish financial responsibility. Thus, they do not include output per head and unemployment rates. In the last paragraph of Article 140, it is stressed that the monitoring reports ‘shall also take account of the results of the integration of markets, the situation and development of the balances of payments on current account and an examination of the development of unit labour costs and other price indices’.

## A. CURRENT ECONOMIC OUTLOOK

To start, figures provided in a previous review undertaken by the Commission during 2012 read as follows:<sup>92</sup>

	Real Gross Domestic Product (GDP) Growth in the EU (2009)	-4.2%
	Unemployment in the EU (Autumn 2010)	9.6%
	General Government deficit in the EU (2009, % of EU GDP)	6.8%
	State aid for banks, including unused guarantees (% of EU GDP)	13%

The current economic situation reveals interesting insights into the state of the economy and eventually justifies bailouts. Inflation has generally been higher than 2%. According to the latest Eurostat figures,<sup>93</sup> the annual *inflation* rate in the Eurozone area was 1.6% in July 2013 compared to 2.4% a year earlier. The annual inflation rate in the European Union was 1.7% in July 2013.<sup>94</sup> Therefore, a country with a relatively low (high) inflation rate has a relatively high (low) real interest rate. However, monetary policy has been operated in a perverse manner, with low

<sup>91</sup> It will be inferred from a rate of inflation which is close to that of the three best performing Member States.

<sup>92</sup> Source: EU Commission, Towards More Responsibility and Competitiveness in the European Financial Sector, 2012.

<sup>93</sup> Eurostat, euro indicators, press release 123/2013, 16 August 2013.

<sup>94</sup> The largest increase to the euro area annual inflation is said to come from fruit, vegetables and tobacco.

real rates being applied where inflation is relatively high. This contradicts the presumption that high inflation is met by high real rates of interest to dampen demand. Many economists agree that compared with the Bank of England and the US Federal Reserve (FED), which have reduced aggressive interest rates, the ECB has adopted a stricter approach. In April 2011, interest rates reached 1.25%. Apart from the existing large current account imbalances between the EMU Member States, there are also substantial differences in terms of changes in unit labour costs.

Unemployment rose to 26.2 million in January 2013, which accounts for 10.8% of the active population<sup>95</sup> and 11.9% of the active population in the euro area (19 million). However, long-term unemployment reached another 'historical high'<sup>96</sup> in the third quarter at 11.2 million, which is 86% higher than four years earlier. It is also worth highlighting that according to Eurostat, youth unemployment reached its peak in January this year with 23.6% of active youths.<sup>97</sup> EU immigration was 20.7 million in January 2012 and EU migration was 13.6 million.<sup>98</sup> In addition, 25.7% of people aged between 55-64 were living in poverty and social exclusion,<sup>99</sup> while the EU lowest average salary was just 393 euros (Bulgaria).<sup>100</sup> In 24 Member States, the likelihood of finding a job was lower in the third quarter of 2012 than four years before.<sup>101</sup>

Major planned cuts in the industry sector cast rather a bleak shadow over the overall economy. For example, in the banking sector, Commerzbank is implementing a global restructuring plan targeting between 4000 and 6000 job losses by 2016; in the airline sector, Iberia is cutting 19% of its entire workforce (3807 employees) and Air Berlin another 900 by 2014,<sup>102</sup> while the manufacturing sector lost 36964 jobs last year, and financial intermediation 19585. In the car industry, Renault announced 7500 job cuts by the end of 2016, and Fiat Poland another 1450 jobs.<sup>103</sup> The worst prognosis is in the construction industry, and wholesale and retail trade as a result of significant reductions in terms of output, added value, and employment.<sup>104</sup>

## B. THE 'EFFICIENCY' JUSTIFICATION AGAINST BAILOUTS OF INEFFICIENT BANKS OR STATES

Article 119 makes it clear that the adoption of an economic policy which is based on the 'close coordination' of Member States' economic policies, on the internal market, and on common objectives has to be in accordance with the principle of an open market economy with free competition. Competition law rarely accepts a failing-firm-defence on the grounds of its poor economic performance, that is, inefficiency. Article 120 also makes it clear that economic policies ought to follow the same principle, 'favouring an efficient allocation of resources'. Furthermore, Article 123 (1) contains an imperative prohibition of 'overdraft facilities or any other type of credit facility with the ECB or with the central banks of the Member States in favour of Union institutions, bodies, offices or agencies, central governments, regional, local or other public authorities, other bodies governed by public law, or public undertakings of Member States' as well as 'the purchase directly from them by the ECB or national central banks of debt instruments'. One cannot possibly comment more on the legally binding hierarchy and 'constitutional' ranking of the above provisions, which clearly eliminate the possibility of granting bailouts on the basis of inefficiency, be it at state or TBTF level, without basically undermining the rule of law and transforming the spirit of free competition into coercive freedom, the meaning of which will be discussed towards the end of this article.

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<sup>95</sup> European Commission, EU Employment and Social Situation Quarterly Rev March (2013) 5. Other high unemployment rates were recorded in Bulgaria (-4.9%), Cyprus (-4.8%) and Spain (-4.5%).

<sup>96</sup> Ibid, 6.

<sup>97</sup> The youth unemployment rate ranges from 15% or more in Austria, Denmark, Germany and the Netherlands to 55% or more in Greece and Spain. Highest unemployment rates were registered in Greece (-6.5%) and Portugal (-4.3%) while their GDP also fell to -6% and -3.8% respectively.

<sup>98</sup> Ibid, 15.

<sup>99</sup> Ibid 24.

<sup>100</sup> Ibid 28.

<sup>101</sup> Ibid 30.

<sup>102</sup> Ibid 66.

<sup>103</sup> Ibid 65.

<sup>104</sup> Ibid, 58.

Competition intervention in favour of TBTF banks has been implemented through crisis communication. It has been argued for some time now that state aid communications bear no legally binding force.<sup>105</sup> Thus, they are implementing administrative provisions and offer guidance on how to deal with the restructuring or capitalisation of banks. Therefore, a higher hierarchical and constitutionally accepted rescue provision is Article 107 (3) b TFEU on state aid to 'remedy a serious disturbance in the economy of a Member State'. This has practically closed the academic debate over the primacy of 'hard' over 'soft' law.<sup>106</sup> Thus, I would call the latter an administrative law which has binding force. No legal act or decision whatsoever would otherwise be enacted if it were to be disregarded. Furthermore, if it were legally valid that 'soft law' communications are not binding on European courts, this would be instrumental, on the one hand, for states to claim disgorgement of profits for cashed bailouts of banks engaged in fraudulent pursuits and, on the other hand, for EU citizens to claim fair compensation through taxation. It would be legitimate for them to pay lower taxes until the almost 40% of the GDP in bailouts was credited on their payroll accounts.

In conclusion, the apparent legitimacy of state bailouts is in the treaty; the implementation of banks bailouts is in administrative law communications.

## V. ON THE SOCIAL COSTS OF THE CRISIS

### A. HOW MUCH STATE AID DO YOU NEED?

Some evolutionary insights into how state aid gradually progressed reveal that between 2002 and 2007, the amount of state aid decreased by 2% annually, i.e. €65 bn or 0.5% of the GDP,<sup>107</sup> followed in 2008 by a nearly four-fold increase to 2.2% of the GDP, of which €279.6 bn was spent on state aid and €212.2 bn on crisis measures, i.e. 1.7% GDP. Between 2008 and 2009, the figure of €3.632 bn, the equivalent of 29% GDP, signalled an alarming shift of perspective when everybody started to 'see red'.

Nevertheless, even 'ad hoc' state aid in favour of individual financial institutions amounted to €587 bn (9% GDP).<sup>108</sup> Member States such as Germany, the UK and France, which make up 60% of the EU banking sector, received 60% of the total amount of state aid granted.<sup>109</sup> A total of 215 financial institutions received some form of aid, but 114 received toxic asset support relief.<sup>110</sup> Between 2008 and 2011, the Commission approved a shocking €4.5 trillion of state aid, that is, nearly 36.7% of the EU GDP.<sup>111</sup> This makes the entire GDP worth €12.26 trillion.<sup>112</sup> Minus the bailouts, the remaining €7.76 trillion is approaching another Great Depression as macroeconomics suggests that at extremely low levels of real GDP, when output is €3 trillion, the economy is in a depression.<sup>113</sup>

The social and economic costs estimated for the UK economy post-intervention are from £1 bn to £3 bn per annum, which means nearly £40 bn of lost output.<sup>114</sup> Other macroeconomic crisis mechanisms, such as the EU

<sup>105</sup> See e.g. T Doleys, 'Managing State Aid in a Time of Crisis: Commission Crisis Communications and the Financial Sector Bailout' 34 J of Eur Integration 6 (2012) 549.

<sup>106</sup> See the comprehensive and insightful contributions on soft law of O Stefan, *Soft law in court: competition law, state aid and the Court of Justice of the European Union* (Kluwer Law Int, 2013); 'Hybridity before the court: a hard look at soft law in the EU competition and state aid case law' 37 European L Rev (2012) 49.

<sup>107</sup> P Nicolaides, 'State aid' in I Kokkoris and R Olivares-Caminal (eds) *Antitrust Law amidst Financial Crisis* (Cambridge, CUP, 2010).

<sup>108</sup> Lyons and Zhu, 47.

<sup>109</sup> Quigley, 240. It is worth recalling that during 2008/09 Germany received €400 in guarantees, €80 in recapitalization, €1.5 liquidity aid, and €107.6 for other individual cases, while UK received respectively €376.75, €63, €11.3 and €61.2 for the same categories of state aid.

<sup>110</sup> Ibid.

<sup>111</sup> Source: DG COMP at [http://ec.europa/competition/recovery/financial\\_sector.html](http://ec.europa/competition/recovery/financial_sector.html). See e.g. Pisani-Ferry and Sapir, n, 358, who mentioned that by the end of August 2009 state aid measures amounted to 44% GDP

<sup>112</sup> See [http://eeas.europa.eu/delegations/gulf\\_countries/press\\_corner/index\\_en.htm](http://eeas.europa.eu/delegations/gulf_countries/press_corner/index_en.htm);  
<http://epp.eurostat.ec.europa.eu/portal/page/portal/eurostat/home/>.

<sup>113</sup> Slavin, 262.

<sup>114</sup> This is why several economists have argued that countries facing insolvency should default as quickly as possible to allow a substantial debt restructuring (haircut) aimed at restoring sustainable debt levels and stabilising financial markets. The UK government spent \$856 bn to support

Stabilisation Mechanism, allow the Commission to raise up to €60 bn as financial assistance to Member States experiencing financial difficulties. The EU Financial Stability Facility has been set up to issue debt securities guarantees of up to €444 bn.<sup>115</sup> Therefore it does not make us feel any better to know that in 2009, the US bailout amounted to \$8 trillion,<sup>116</sup> that is \$30,000 per citizen, \$650 bn of GDP income, 5.5 million jobs, \$360 bn in wages etc.<sup>117</sup> This has made academics suggest that instead of rewarding those institutions that caused the crisis, it would have been much better to write a \$120,000 cheque to a household of four to keep up with their mortgage payments. Recent figures contradict a 2009 estimate by the International Monetary Fund of \$11.9 trillion as the total cost of the global crisis.<sup>118</sup>

It is by no means controversial to say that banks were being favoured before the current crisis hit. Banks were immune from competition intervention and allowed to merge, which is another fact that is statistically documented. Between 1997 and 2007, the number of EU banks declined by 29% compared to 22% in the US.<sup>119</sup> Bank concentration levels remain relatively high post-crisis, while recent research contradicts the economic assumption that concentration levels should necessarily translate into high market shares.<sup>120</sup> Against the shortcoming of immunity to competition agency scrutiny,<sup>121</sup> it does not follow that banks did not compete against each other. Another telling fact is that it is precisely tougher competition that has increased the risk-taking incentives of banks and pushed them to pursue risky portfolios.<sup>122</sup> Shareholders have designed compensation contracts to insure managers against failure and incentivize risk-taking. Therefore, keeping this numeracy exercise in mind is essential when questioning how state aid has been spent on banks.

## B. MAIN CATEGORIES OF CRISIS STATE AID

So far the EU has offered €2,738 bn in bank guarantee schemes, €231 bn in the form of the recapitalisation of banks, and €76 bn in the form of general liquidity measures and asset relief. The crisis of state aid emerged following the collapse of Lehman Brothers. The first €26 bn bailout went to the German IKB and Sachsen LB, which had been exposed to asset-backed securities in the US subprime market. This was followed by the UK bailout of Northern Rock, late 2007 and early 2008. Then, WestLB, Fortis and Dexia followed. The Irish Daily offered €400 bn as a guarantee scheme to cover retail, commercial, and interbank deposits.

The Commission's crisis reaction was to issue an administrative act, the *Banking communication*,<sup>123</sup> following which

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the crisis in 2008; see Clarke 44.

<sup>115</sup> Source: European Commission, MEMO/12/413, Brussels 6 June 2012. Other notable aids include €50 bn to the Hellenic Stability Financial Fund for the purpose of bank capitalisation; €12 bn of the Bank Solvency Support Facility in Portugal marked on a dedicated account at the central bank; €600 mill for Latvian banking support.

<sup>116</sup> Thus Moseley reports \$700 bn in order to bail out US banks; see F Moseley, 'The Bailout of the 'Too-Big-to-Fail' Banks: Never Again' in *Handbook* (2013) 645.

<sup>117</sup> See e.g. 'The Nature and Effects of the 2007-2010 Crisis and Ways to Resolve it' in R Macdonald, *Genesis of the Financial Crisis* (London, Palgrave Macmillan, 2012).

<sup>118</sup> W Sun, J Stewart and D Pollard, 'Introduction: rethinking corporate governance –lessons from the global financial crisis' in Sun, Stewart and Pollard (eds) *Corporate Governance and the Global Financial Crisis: International Perspectives* (Cambridge, CUP, 2011).

<sup>119</sup> X Vives, 'Competition policy in banking' 27 *Oxford Rev of Economic Policy* 3 (2011) 482.

<sup>120</sup> Scherer 10.

<sup>121</sup> For example, the US Dodd-Frank Act of July 2010 prohibited any merger or acquisition which results in a combined market share of more than 10% of domestic deposits, the concentration limit on any consolidation being 10% of financial industry liabilities. This Act aims to promote the financial stability of the US, by improving accountability and transparency in the financial system, to protect the American taxpayer by ending bailouts, and to protect consumers from abusive financial services practices.

<sup>122</sup> Vives 485.

<sup>123</sup> Communication from the Commission –The Application of State Aid Rules to Measures Taken in Relation to Financial Institutions in the Context of the Current Global Financial Crisis, OJ C 270/8 of 25 October 2008, departs from its predecessor EC Guidelines on State Aid for Rescuing and Restructuring Firms in Difficulty, OJ C 244/2 of 1 October 2004. The latter allowed the Commission to distinguish among guarantees, recapitalizations, impaired assets measures, as aid modalities, and their recipient, distressed firms. The Banking Communication



it received notifications for guarantee schemes, recapitalization, and other interventions of up to €2 trillion.<sup>124</sup> This aid was still insufficient to restore market confidence as bank balance sheets continued to erode. The ECB intervened through liquidity operations. The Commission's disagreement with French institutions over 'preventive recapitalization' caused alarm bells to ring in that there were some serious doubts over whether €10.5 bn<sup>125</sup> was, indeed, offered to TBTF banks. In this context, the Commission issued its *Recapitalization communication*,<sup>126</sup> which provided guidance on the pricing of capital injections. It distinguished between 'distressed' and 'fundamentally sound' banks.<sup>127</sup> The former were required to pay higher coupon rates.

Following German plans to create a series of special purpose vehicles (SPV) and a heated debate over assets pricing, the Commission issued its *Impaired assets communication*<sup>128</sup> to handle toxic assets. Asset relief in the form of asset purchase has meant that the state would buy the impaired asset portfolio at a fixed price, but higher than the market price. On the basis of toxic asset guarantees, the State has practically taken over a share of the default risk and losses.<sup>129</sup> The conditions for granting such aids required full disclosure of the assets; sharing the cost between Member States, shareholders and creditors, and coordination among them; and restructuring distressed banks.<sup>130</sup> The German scheme allowed financial institutions to transfer structured securities to a 'special purpose vehicle' for a period of 20 years and bear the full risk of losses.

Another *Restructuring communication*<sup>131</sup> targeted banks with unsustainable business models. Banks were required to demonstrate their own strategies to achieve long-term viability without State aid under adverse economic conditions, known as a bank 'stress' test.<sup>132</sup> The restructuring of banks began with Commerzbank,<sup>133</sup> which had previously received €18 bn from the German government. The bank was required to divest itself of its investment banking and real estate and accepted a short-term ban on acquisitions. Its overall business contracted *ex post* at approximately €500 bn (45%).<sup>134</sup> Other restructured banks included RBS, Lloyds, Anglo Irish Bank, Fortis, Dexia, Bayern LB, HSH Nordbank, IKB, West LB, ING and ABN Amro.

As Lyons and Zhu have rightfully commented, the above 'zombie' banks 'absorb savings and withdraw lending as they rebuild their own capital, to the detriment of lending to the non-financial sector',<sup>135</sup> thereby contributing to the current recession. Another excellent point to make is the need to reform any banking system that 'privatises profits and socialises losses'.<sup>136</sup> The EU intervention in the banking sector, on the basis of its flawed TBTF doctrine of state intervention in the economy, has transferred the economic responsibility of inefficient corporations to the social responsibility of individual taxpayers.<sup>137</sup>

The above developments in administering state aid have practically changed the whole structure of the banking sector in a way which has substantially departed from the traditional prevention of distortions of competition. The

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made possible the authorisation of state aid in the form of guarantees, capital, asset relief or liquidity on a non-discriminatory basis, for a limited time and scope, see e.g. Quigley 239.

<sup>124</sup> Doleys 556.

<sup>125</sup> Doleys 558.

<sup>126</sup> Communication from the Commission – The Recapitalisation of Financial Institutions in the Current Financial Crisis: Limitation of Aid to the Minimum Necessary and Safeguards against Undue Distortions of Competition, OJ C 10/2 of 15 January 2009.

<sup>127</sup> Quigley 239; see also T Franchoo and M Pollard, 'The Application of European Competition Law in the Financial Services Sector' J of European Comp Law & Practice (2012).

<sup>128</sup> Communication from the Commission on the Treatment of Impaired Assets in the Community Banking Sector, OJ C 72/01 of 26 March 2009.

<sup>129</sup> Quigley 239.

<sup>130</sup> Ibid.

<sup>131</sup> Commission Communication, The return to viability and the assessment of restructuring measures in the financial sector in the current crisis under the State aid rules, OJ 2009 C 195/9.

<sup>132</sup> Quigley 239.

<sup>133</sup> Commerzbank case N 625/2008; see e.g. Heimler and Jenny 364 criticisms on the imposition by the Commission of limitations on managers' compensation and severance packages.

<sup>134</sup> Doleys 561.

<sup>135</sup> B Lyons and M Zhu, 'Compensating Competitors or Restoring Competition? EU Regulation of State Aid for Banks during the Financial Crisis' 13 J of Industrial Comp and Trade (2013) 45.

<sup>136</sup> Ibid 47.

<sup>137</sup> See FM Scherer, 'A Perplexed Economists Confronts 'Too Big to Fail'' 7 Eur J of Comparative Econ 2 (2010) 267.

next question to ask, therefore, is not whether competition enforcers have not been prepared to undertake this mission, because, obviously, they weren't, but to ask how much state aid has been taken away from the overall prospects of economic growth in terms of GDP and weighted against, as mentioned earlier, the rising unemployment in the EU and the passing on of social costs through taxation. Finally, this revolutionary change of perspective makes competition law and policy the scapegoat of a New Banks Deal. Its story of success for banks and failure for citizens has been possible on the basis of the Union's democratic deficits, since its citizens have no say in the next election of the President or of the College of Commissioners, both of which have been instrumental in matters of competition policy.<sup>138</sup> This point uncovers an existing *institutional* crisis; for example, the European Commission's plans to create an agency to rescue or shut failed banks by 2015 against the significant backdrop of not having a European banking union until January 2014, after the general elections in Germany.<sup>139</sup> The latter aspect pinpoints the politics of the crisis. Recent research suggests that, for a number of reasons, electoral competition is likely to constrain the abuse of public resources in the form of bailouts.<sup>140</sup> This is fully evidenced in the following criticism by a member of Socialists and Democrats (Elisa Ferreira) who said: 'We need to stop casino banking, break the link between public finance and failing banks, and ensure sustainable financing of the real economy to encourage growth'. As Wibbels rightfully put it when investigating the constitutional dimension of crisis bailouts,<sup>141</sup> the above statement based on 'competitive politics' encourages what one would call famously in competition a way of 'publicly distancing oneself'<sup>142</sup> from the culprit of bailouts. Electoral competition should actively discourage zombie banks from looking at the welfare state as their lender of last resort. In conclusion, what this bitter 'crisis' has taught us, so far, is that structural changes happen during a crisis whenever state intervention is insufficiently backed up by constitutional and institutional safeguarding mechanisms since it is easier to abuse the rule of law on the basis of predicted, imminent economic downturn.

### C. STATE AID FOR NON-CHAMPION BANKS<sup>143</sup>

The following table illustrates who are the top 'zombie' bank beneficiaries.

<input checked="" type="checkbox"/>	<b>TBTF BANKS</b>
✗	rescue aids: Hypo Real Estate Holding, Commerzbank, WestLB;
✗	restructuring: Sachsen LB, IKB, West LB, Landesbank Baden Württemberg, Sparkasse KölnBonn, Hypo Real Estate, HSH Nordbank, NordLB, Bayern LB;
✗	WestLB €3 bn capital injections, €11 impaired assets of which €3.4 bn. <sup>144</sup>
✗	Anglo Irish Bank €29.3 bn
✗	Irish Nationwide Building Society (INBS) €5.4 bn;
✗	Hypo Real Estate €9.95 bn in capital injections, €145 in guarantees and €20 bn in asset relief;
✗	ING €17 bn
✗	Fortis Bank €11.2 bn

<sup>138</sup> In contrast, architectural differences did not allow the US antitrust enforcers to administer bailouts through means of antitrust policy; see e.g. the Remarks of Bert Foer, President of the American Antitrust Institute, 'Competition Policy and 'Too Big' Banks in the European Union and the United States', June 27, 2013.

<sup>139</sup> Source: EurActiv, New banking authority pits Commission against Berlin, 11 July 2013 available at <http://www.euractiv.com/print/euro-finance/new-banking-resolution-authority-news...>

<sup>140</sup> E Wibbels, 'Bailouts, Budget, and Leviathans: Comparative Federalism and Lessons from the Early United States' 36 Comparative Political Studies (2003) 486.

<sup>141</sup> Wibbels 487.

<sup>142</sup> To quote David Bailey's excellent article on 'Publicly Distancing Oneself from a Cartel' 31 World Comp 1 (2008) 177.

<sup>143</sup> For an overview of decisions and ongoing in-depth investigations in the context of the financial crisis, see European Commission, Brussels, 20 December 2012, available at [http://europa.eu/rapid/press-release\\_MEMO-12-1018\\_en.htm](http://europa.eu/rapid/press-release_MEMO-12-1018_en.htm)

<sup>144</sup> The state aid was said to be incompatible with the restructuring communication as it exceeded the real economic value of this banks' assets.

#### D. FAMOUS GOVERNMENT BAILOUTS IN THE UNITED KINGDOM

*Northern Rock* (fifth largest UK mortgage bank with a 9.7% market share of UK gross mortgage lending (18.9% net)<sup>145</sup> received £20 bn as a retail deposit guarantee scheme plus a further £25 bn liquidity facility from the Bank of England. There is disagreement over whether *Northern Rock* was a systemically important bank since it did not trigger problems elsewhere in the banking system.<sup>146</sup> Elsewhere, it has been argued that it was precisely the Bank of England's intervention that did not allow this to happen. Unfortunately, NR created a precedent of intervention on the basis of TBTF. It is also useful to recall here that the ECB identified some 46 systemically important banks which account for 68% of EU banking.<sup>147</sup> This is the result of allowing mega-mergers to go ahead<sup>148</sup> and the monopoly power of banks on business lending.<sup>149</sup>

*Royal Bank of Scotland (RBS)* received £45 bn to ensure its survival because the bank was under-capitalised, failed to maintain adequate liquidity, and was involved in a risky financial strategy. It had previously participated in a consortium along with Fortis and Santander to acquire ABN AMRO.<sup>150</sup>

*Lloyds TSB/HBOS*, as a result of a rescue merger with HBOS,<sup>151</sup> received £17 bn state recapitalisation in January 2009<sup>152</sup> (the UK government has recently sold part of its 43.5% equity ownership), with £260 bn of toxic assets temporarily insured. According to the OFT (2010), Lloyds was the second largest bank with 30% market shares in personal current accounts and a 24% market share in gross mortgage lending, while HSBC had only 16% and 13% respectively.<sup>153</sup> Because of restructuring aid received largely as a result of its acquisition of HBOS,<sup>154</sup> Lloyds and RBS are required to divest a 5% market share to a new entrant, or small existing competitor in the market and achieve a £181 bn reduction of assets by 31 December 2014.<sup>155</sup>

During mergers investigations in the banking sector, the Commission can request all relevant information from the national supervisory authorities. Thus, Member States may block a merger in order to protect a 'legitimate interest', such as financial stability in the domestic market, leaving some discretionary power to national supervision authorities. In contrast, the US DoJ cannot review a merger for systemic risk.<sup>156</sup> However, competition authorities ought to be prudent when accepting the failing-firm-defence for under-performing, inefficient, and poorly managed firms.<sup>157</sup> Otherwise, the TBTF doctrine becomes moral hazard.

One cannot reflect on the above famous bailouts without formulating the following question: what did these banks have in common? The answer is a very fragile funding model supported by a risky loan portfolio and the fact that, in their rescue, the Commission did not come up with a pertinent 'counterfactual'<sup>158</sup> scenario of what would have happened if they had been allowed to fail. Fortis<sup>159</sup> is yet another example of bank rescue due to excessive risk taking

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<sup>145</sup> Lyons 49.

<sup>146</sup> Ibid 51.

<sup>147</sup> European Central Bank (2006 and 2008), EU Banking Structures, Frankfurt am Main.

<sup>148</sup> See Stucke 318 who points at the post-merger consolidated assets of \$751 billion and the US mega-merger, Travelers Group Inc and Citicorp; Markham 291 pinpointing that between 1980 and 1999, the number of commercial banks declined from 15000 to just 9000; HA Shelanski, 'Enforcing Competition During an Economic Crisis' 77 Antitrust LJ (2010-2011) 238.

<sup>149</sup> MH Wolfson, 'An Institutional Theory of Financial Crisis' in *Handbook* (2013) 183.

<sup>150</sup> Akinbami (2013) 23.

<sup>151</sup> Prior to its takeover, HBOS was collapsing because of its high-risk lending practices and excessive use of leverage. Therefore, LBS's takeover offer was conditional upon the receipt of a large amount of government aid necessary to rescue HBSO. See Marsden and Kokkoris 889.

<sup>152</sup> Figures are slightly contradicted by R Tomasic, 'The failure of corporate governance and the limits of law: British banks and the global financial crisis' in Sun, Stewart and Pollard (eds) 59, relying on the House of Commons Treasury Committee, 'Banking Crisis: Dealing with the Failure of the UK Banks: Seventh Report of Session 2008-09', London, 519. Namely, £31.6 bn for Lloyds-TSB, £39.30 bn for HBOS, £47.1 bn for Barclays, £62.8 bn for RBS and £103.1 bn for HSBC.

<sup>153</sup> Vives 493. However, Lloyds was not allowed to take over Abbey in 2001.

<sup>154</sup> The UK gave notification of a restructuring plan for Lloyds Banking Group on 16 July 2009.

<sup>155</sup> Quigley 245; see also P Marsden and I Kokkoris, 'The Role of Competition and State Aid Policy in Financial and Monetary Law' 13 JIEL (2010) 3, 877.

<sup>156</sup> Stucke 322.

<sup>157</sup> See e.g. Marsden and Kokkoris 881.

<sup>158</sup> See also Lyons 54 on WestLB.

<sup>159</sup> On Fortis case, see e.g. J Pisani-Ferry and A Sapir, EU banking policies, Economic Policy, April 2010, 354.

as a result of its participation in the ABN AMRO merger.<sup>160</sup> Competition authorities have been ill-equipped to assess the systemic risk and eroded the legitimacy of the TBTF doctrine of intervention as it has helped inefficient banks to remain 'viable' on the market.<sup>161</sup> Even the Commission itself has practically realised its defective implementation since, more recently, it has called for a 'sound' restructuring plan for banks before capitalisations or taking any other asset protection measures.<sup>162</sup> This new move follows early indications that the EU is going to 'toughen' its state aid to failing banks.<sup>163</sup> Given such a huge social cost to society, the new approach comes late. The major criticism of the TBTF doctrine remains, however, it having been endorsed by EU policy-makers as a 'way out' of the crisis.

## VI. ON EMERGING ANTI-COMPETITIVE PRACTICES RELATED TO THE TBTF DOCTRINE

Most recent antitrust investigations have dealt with innovative and highly sophisticated financial contracts, such as securitization, credit default swaps (CDS) or repos. They have affected businesses and consumers at a micro economic level.<sup>164</sup> It was estimated that as the world GDP was \$65 trillion in 2007, the value of the companies listed in the world stock markets would reach \$63 trillion, but the total value of financial derivatives was \$596 trillion, that is, eight times the size of the real economy,<sup>165</sup> with a growth rate of 32% per annum since 1990.<sup>166</sup>

*Securitization* is a highly sophisticated process of pooling high risk debt assets from residential mortgage loans, car loans, credit cards and so on, which were sold to an SPV in return for securities.<sup>167</sup> Put simply, this process makes sure that risks associated with loans are shifted away from the original lenders to investors. First, the originator (O) applies for a mortgage loan; then the SPV buys O's mortgage to guarantee the remoteness of the cash flows in return for securities which are purchased by investors (I). The cash received from I pays O's loan. Basically, any interest rate or currency risk associated with the pooling of such assets is hedged<sup>168</sup> using a variety of credit swap transactions. Credit rating agencies<sup>169</sup> have played a key role in boosting the attractiveness of such securitized assets by assigning a credit rating for securities issued via the SPV. Investors have been overly reliant on ratings. In *collateral bonds*, the default risk has also been insured through CDS, i.e. the client promises to pay the guarantor a fixed fee in exchange for the guarantee that if a bond defaults, the guarantor will redeem it.

*Credit default swaps* are derivative contracts designed to transfer the risk of credit default on debt obligations.<sup>170</sup> CDS are used by investors as an investment vehicle to hedge assets against default risks and assess debtor's creditworthiness. Previously, the Commission has issued guidance on how to calculate the pricing of capital injections to 'rescue' CDS.<sup>171</sup> However, very recently, the Commission sent a statement of objections to 13 investment banks,

<sup>160</sup> On unsustainable business models see e.g. Lyons 58.

<sup>161</sup> See also A Heimler and F Jenny, 'The limitations of European Union control of state aid' 28 *Oxford Rev of Economic Policy* 2 (2012) 358 both of whom are critical on restructuring aid being offered to 'inefficient firms to remain active in the market'.

<sup>162</sup> European Commission, IP/13/672, Brussels, 10 July 2013, 'State aid: Commission adapts crisis rules for banks'.

<sup>163</sup> Bloomberg, J Brunsden and E Duarte, 'EU to Toughen Creditor-Loss Rules at Failing Banks' August, 8 July 2013, at <http://www.bloomberg.com/news/print/2013-07-08>, where it is mentioned that the EU has spent €1.7 trillion on the basis of the TBTF doctrine.

<sup>164</sup> See the Commission's 'new' mission: 'Competition law should ensure that credit institutions and other financial service providers do not behave in a manner that hampers the efficient functioning of the internal market', at [http://ec.europa.eu/competition/sectors/financial\\_services/capital\\_markets.html](http://ec.europa.eu/competition/sectors/financial_services/capital_markets.html)

<sup>165</sup> Sun, Stewart and Pollard 9.

<sup>166</sup> T Clarke, 'Corporate governance causes of the global financial crisis' in *Handbook* (2012) 31.

<sup>167</sup> See also BJ Keys, TK Mukherjee, A Seru and V Vig, 'Did Securitization Lead to Lax Screening? Evidence from Subprime Loans' 125 *Quarterly J of Economics* 1 (2010) 307; S Krishnan, 'Securitization' in *Handbook* (2012) 290.

<sup>168</sup> Hedge funds are collective investments with a wide range of objectives, strategies, styles, techniques and assets, normally open to selected institutions.

<sup>169</sup> For example, Standard & Poor's, Moody's and Fitch.

<sup>170</sup> See C Brummer, *Soft Law and the Global Financial System: Rule Making in the 21<sup>st</sup> Century* (Cambridge, CUP, 2012) 212: The protection buyer is entitled to receive from the protection seller the par value of the bond on which the contract was made should the third party borrower default on its payments.

<sup>171</sup> Source: Communication from the Commission on the application of State aid rules to support measures in favour of banks in the context of the financial crisis, OJ C 356/02 2011. The guarantee fee should be the sum of a basic fee of 40 points, a risk-based fee to the product of 40 points and a risk metric composed using the following formula: the guarantee fee = 40bp x (1 + (1/2 X A/B) + (1/2 X C/D)), where A is the beneficiary's median five-year senior CDS spread; B is the median iTraxx Europe Senior Financials five-year index; C is the median five-year

which have acted as intermediaries in the market for credit derivatives.<sup>172</sup> Another investigation into CDS targets the International Swaps and Derivatives Association involved in the over-the-counter (OTC) trading of derivatives.<sup>173</sup> Preliminary indications suggest that the association may have been involved in a coordinated effort of investment banks to 'delay or prevent exchanges' from entering the credit derivatives business. An excellent definition of derivatives is offered by Braithwaite.<sup>174</sup> Derivatives are 'bilateral contracts where the rights and obligations of the parties reference an underlying asset, benchmark, index or other variable'. The classic example is a CDS where A and B decide on a notional sum. A agrees to pay B a fixed interest rate on that sum (periodic payment) while B agrees to pay a variable rate in return. As a result, B, who has a variable rate income but a fixed rate debt, can swap income streams with counterparties.<sup>175</sup>

Over-the-counter derivatives (OTC), estimated at \$707 trillion, are the reason why Lehman Brothers collapsed.<sup>176</sup> The number of OCTs rose to nine times the world GDP in 2010.<sup>177</sup> There are some 65 million derivative contracts which are privately negotiated and used, for example, to hedge interest rates and credit risk, minimise tax liabilities or speculate on currencies etc.<sup>178</sup> Hedging implies a transfer of assets with the aim of generating better returns to a given level of risk.<sup>179</sup>

A repo is a collateralized loan where the seller agrees to sell securities at a discount (haircut) to the buyer (lender).<sup>180</sup> Lenders are rich institutional investors, like pension funds and mutual funds, that need a liquid but relatively safe place to invest cash. Repo is a generic name for repurchase agreements and sell/buy-backs, namely, A sells an asset (usually fixed-income securities) to B at price X. A also commits itself to repurchase the asset from a third party, C, at price Y in the near future or on demand.<sup>181</sup> In other words, in the event that A defaults, B can sell it to C to offset its loss. Despite being labelled as the sale and repurchase of securities, repo is economically a 'secured deposit' having as its purpose the borrowing and lending of cash.

All of the above are characterized by an oligopoly pricing power, asymmetric information, and unequal bargaining power, which allowed banks to generate high profits.<sup>182</sup> The proliferation of these contractual instruments demonstrates the value of Minsky's classification of 'financial fragility'<sup>183</sup> as (i) hedge finance which amounts to liability obligations to be paid with the net cash flows from routine transactions; (ii) speculative finance where cash reserves are insufficient and require borrowing funds or selling less-liquid assets; and (iii) Ponzi finance where there will never be enough cash to meet outstanding financial obligations.<sup>184</sup> Due to a failure to obtain additional financing, Ponzi firms have had to sell their assets, which created Fisher's 'price deflation'<sup>185</sup> for the firms' assets.

## VII. ON THE LIBOR MANIPULATION SCANDAL: YET ANOTHER ANTI-COMPETITIVE PRACTICE?

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senior CDS spread of all Member States; D is the median five-year senior CDS spread of the MS granting the guarantees. In other words, the risk profile in recapitalisation state aid is measured through the media five-year senior debt CDS spread.

<sup>172</sup> European Commission, IP/13/630, Brussels, 1 July 2013. The 13 banks are Merrill Lynch, Barclays, Bear Stearns, Paribas, Citygroup, Credit Suisse, Deutsche Bank, Goldman Sachs, HSBC, Morgan, Morgan Stanley, RBS, UBS and ISDA.

<sup>173</sup> European Commission, IP/13/286, Brussels, 26 March 2013.

<sup>174</sup> JP Braithwaite, *Standard Form Contracts as Transnational Law: Evidence from the Derivatives Markets*, 75 MLR 5 (2012) 783.

<sup>175</sup> Ibid 784.

<sup>176</sup> Ibid 785, 789. Lehman Brothers is said to have been involved in over 2,000 derivatives transactions. Five firms dominate the European and American OTC derivatives market, see Scherer 14.

<sup>177</sup> GA Epstein and P Habbard, 'Speculation and Sovereign Debt: An Insidious Interaction' in *Handbook* (2013) 328.

<sup>178</sup> Ibid.

<sup>179</sup> P Lysandrou, 'Hedge funds' in *Handbook* (2012) 145.

<sup>180</sup> JS Taub, 'What We Don't Talk About When We Talk About Banking' in *Handbook* (2013) 457.

<sup>181</sup> See European Commission, Directorate-General for Internal Policies, Policy Department Economic and Scientific Policy, Economic and Monetary Affairs, Note on Shadow Banking-Minimum Haircuts on Collateral, 2013, 56.

<sup>182</sup> Crotty 153.

<sup>183</sup> J Kregel, 'Political Economy Approaches to Financial Crisis: Hyman Minsky's Financial Fragility Hypothesis' in *Handbook* (2013) 160.

<sup>184</sup> See Tymoigne 99.

<sup>185</sup> I Fisher, 'The debt-deflation theory of great depressions' 1 *Econometrica* 4 (1933) 337.

LIBOR is a reference index sponsored by the British Banking Association used to calculate short-term interest rates on a range of financial instruments in excess of \$350 trillion, including CDS and complex derivatives.<sup>186</sup> Its daily submission indicates what each bank estimates is their cost of unsecured borrowing from another bank. Competition authorities worldwide (EU, the UK, the US, Canada and Japan) alleged that the Contributor Panel Banks exchanged information to undervalue daily submissions and that brokers colluded to manipulate LIBOR to raise the profits from certain derivatives. In other words, under competitive conditions, banks would submit their valuation independently to move away from forms of artificial collusion. In the US *USD LIBOR* scandal,<sup>187</sup> antitrust damage claims were rejected on the grounds of failure to prove conspiracy and restraint of trade, lack of antitrust standing and impossibility of recovery on the basis of the 'indirect purchaser rule'.<sup>188</sup> The US court ruled that there cannot be a damage recovery without showing that the actual loss stems from a reduction of competition or that any harm is the result of the defendant's behaviour.<sup>189</sup> This interpretation endorses the traditional approach to antitrust harm which requires proof of a resulting restriction of competition in the market for interbank loans. Since LIBOR displays only information about 'prevailing rates', the court went on to say that LIBOR quotations, even in the event that they were set artificially, did not correspond to the actual interest rate charged for interbank loans. This legal reasoning lacks a great deal of pragmatism since the authors of this innovative anticompetitive practice are banks which have unfortunately been excluded from antitrust scrutiny. This fact also justifies the court's reservation. Semantically different from the economics of collusion, the manipulation of exchange rates is one of the means used to deceive the bank panel and implement fraud.

Recent investigations have enquired whether the submitting banks intentionally undervalued LIBOR submissions, whether traders at banks and hedge funds tried to influence the rate to speculate on interest rate derivatives, and whether traders employed within Contributor Panel Banks received information about rates, either directly or through intermediaries, such as inter-dealer brokers. The heated question has turned to whether LIBOR should be assimilated into anticompetitive practices such as price-fixing and be criminalized as are cartels.<sup>190</sup> Exchange rate manipulation has been unknown as an anticompetitive practice, while the banking sector has been practically excluded from any competition intervention against what is known as collusion by brokers/bank panels against consumers to fix the market price artificially.

Another case involves Barclays,<sup>191</sup> which submitted low Dollar LIBOR as a result of management instructions, which began in late August 2007. The Commission and the UK Financial Services Authority (FSA) investigated Barclays' alleged infringements between traders and rate setters for the Euro Interbank Offer Rate (EURIBOR), such as manipulating energy prices in California between 2006 and 2008; mis-selling interest rate swaps to small businesses including fish and chip shops; and mis-selling payment protection insurance. Recently, the Financial Conduct Authority (formerly FSA) stated that Barclays, HSBC, RBS and Lloyds mis-sold insurance to small businesses as credit interest rate swaps. These products were marketed as low-cost protection against rising interest rates.<sup>192</sup> In practice, information asymmetries between informed contract holders and ordinary investors are said to result in price inefficiency,<sup>193</sup> with clear evidence that the share prices of banks were artificially altered by the short selling of derivatives. Specifically, a manipulator sells the shares of a company short and then spreads negative rumours about the company's prospects.<sup>194</sup> This has led to calls for another European proposal introducing bans on naked short

<sup>186</sup> Source: CNN MONEY, A Petroff, Libor moving to NYSE Euronext at

<http://money.cnn.com/2013/07/09/investing/libor-nyse-uk/index.html?section=money...> accessed on July 13, 2013. See C Lim, 'Libor, Strategy, and International Cartel Investigations' JECLP (2013).

<sup>187</sup> See PDS Phillip and RP Girnys, 'No Antitrust Injury in Libor Rate-Setting? –What Happened to Effects?' Comp Policy Int (2012) 3.

<sup>188</sup> Established in *Illinois Brick Co v Illinois* 431 US 720 (1977).

<sup>189</sup> Following a ruling by Judge Naomi Reice Buchwald of the United States District Court for the Southern District of New York.

<sup>190</sup> A Stephan, 'Should Libor-Rigging be treated like Price Fixing?' at

<http://competitionpolicy.wordpress.com/2012/07/11/should-libor-rigging-be-treated-like-price-fixing/>; extremely interesting on crisis cartels A Stephan, 'Price Fixing in Crisis: Implications of an Economic Downturn for Cartels and Enforcement' 35 World Comp (2012) 3, 511.

<sup>191</sup> It is UK's most complained about bank with nearly 12,000 complaints in last six months of 2011 according to the Financial Ombudsman Service.

<sup>192</sup> Source: The Guardian <http://www.guardian.co.uk/business/2013/feb/05/barclays-1-billion-mis-selling-compensation-bill>.

<sup>193</sup> B Clarke, 'Where was the 'market for corporate control' when we needed it?' in Sun, Stewart and Pollard (eds) 77.

<sup>194</sup> Ibid 78.



selling if the price of a financial instrument falls by a significant amount in a single day.<sup>195</sup>

The above recent investigations and the determination of antitrust enforcers and policy makers<sup>196</sup> to deal with the complex and sophisticated financial anti-competitive practices are other indications that the TBTF<sup>197</sup> doctrine is being constantly eroded.<sup>198</sup>

### VIII. END OF STORY: END OF CRISIS?

Finally, it is not possible to understand the dimension of the current crisis without a proper critique of the role neoliberalism has played. Neoliberalism has probably been mostly under-estimated. It is known that neoliberalism called for the deregulation of financial markets<sup>199</sup> in the first instance and for a weak state.<sup>200</sup> Neoliberalism departs fundamentally from ordoliberal ideas of individual freedom as coerced by the state, or as Bonefeld put it,<sup>201</sup> this 'ordered freedom' positions itself somewhere between collectivism and *laissez-faire* liberalism, as a true guardian of markets. As the ordoliberal ideology emerged from attempts to address the problems created by the economic crisis in the 1920s, it has led to a different model of liberal governance, which is generally distrustful of markets. In other words, ordoliberalism was originally packaged as a hybrid product which has prided itself on being sympathetic (a 'humane' economy)<sup>202</sup> to the sociological effects of industrialisation and market competition on workers. However, Rüstow seems, partially, to contradict the human economy at least for 'unionised workers' who threaten the 'weak' state.<sup>203</sup> His ideas hold water as regards pressure groups, such as lobbyists, monopolists or even oligopolists. For Eucken, in contrast, the 'well-being of capitalism' is almost synonymous with being competitive, risk-taking and self-responsible.<sup>204</sup> In other words, it is inconceivable that where the entrepreneurial spirit fails in practice, society should take on the responsibility for such a failure. This is precisely the rather hidden message of the 'social market economy' according to Bonefeld,<sup>205</sup> namely, a social policy that ensures that individuals act as self-responsible entrepreneurs. Applied to our crisis scenario, the big players of speculative games will have to agree to demonstrate social and corporate responsibility if, as Vanberg put it,<sup>206</sup> such players 'systematically' perform poorly.

<sup>195</sup> See EU Regulation no 236/2012 on Short Selling and certain aspects of credit default swaps, which came into force on 1 November 2012, OJ L 86/1.

<sup>196</sup> See an encouraging prospect by Chancellor George Osborne, available at <http://m.guardian.co.uk/business/2013/feb/04/george-osborne-investment-banks-warning>  
<http://www.guardian.co.uk/business/video/2013/feb/04/george-osborne-banking-reforms-video>

<sup>197</sup> D Bush, 'Too Big to Fail: The Role of Antitrust in Distressed Industries' 77 Antitrust LJ 277 (2010); A Mateus, 'Too Big to Fail': Banking Regulatory Reform and What Still Needs to be Done' 7 Comp Policy Int 22 (2011); JW Markham, 'Lessons for Competition Law from the Economic Crisis: The Prospect for Antitrust Responses to the 'Too Big to Fail' Phenomenon' 16 Fordham J Corporate & Financial Law 261 (2011). The concept of TBTF was first applied in the US by Treasury Secretary, William Gibbs McAdoo, to rescue the municipal government of New York City in 1914.

<sup>198</sup> Against TBTF, see e.g. LH Rockwell: 'Don't Bail Them Out', September 10, 2008: 'What should have happened in 1929 is precisely what should happen now. Let the price system prevail! The government should completely remove itself from the course of action and let the market re-evaluate resource values. That means bankruptcies, yes. That means bank closures, yes. But these are part of the capitalistic system,' available at <http://mises.org/daily/3104>; or F Shostak, 'The Rescue Package Will Delay the Recovery', September 29, 2008: 'The government package is not going to rescue the economy, but it will rescue activities that the economy cannot afford and that consumers do not want. It will sustain waste and promote inefficiency, draining resources from growth and efficiency' at <http://mises.org/daily/3131>.

<sup>199</sup> On the deregulation of swaps markets, see M Greenberger, 'Derivatives in the Crisis and Financial Reform' in *Handbook* (2013) 473 in the US through the Commodity Futures Modernization Act of 2010 which removed OTC derivatives transactions from exchange trading and clearing requirements.

<sup>200</sup> See e.g. W Bonefeld, 'Freedom and the Strong State: On German Ordoliberalism' 17 New Political Economy 5 (2012) 635.

<sup>201</sup> Ibid 639.

<sup>202</sup> A Rüstow, 'General Social Laws of the Economic Disintegration and Possibilities of Reconstruction' in *Afterword to Röpke, W. International Economic Disintegration* (London, W Hodge, 1942); W Röpke, *A Human Economy* (Wilmington Delaware, ISI Books) 1998.

<sup>203</sup> Rüstow 276.

<sup>204</sup> W Eucken, 'Staatliche Strukturwandlungen und die Krise des Kapitalismus' 36 Weltwirtschaftliches Archiv (1932) 297.

<sup>205</sup> Bonefeld 647.

<sup>206</sup> V Vanberg, 'Ordnungstheorie' as Constitutional Economics, The German Conception of a 'Social Market Economy' 39 ORDO (1988) 26.

However, for Röpke, the challenge of capitalism lies in the measure of state intervention, i.e. a ‘crisis of interventionism’.<sup>207</sup> This is also true for the EU crisis. Academics seem to agree more and more on one vital point: the real disaster did not happen because banks started to fail, but because the EU and national states rescued precisely those national champions of poor performance and, in the case of toxic assets, of fraud.

The final question after the assessment of law in action and neoliberal policy, as has been implemented in real life, is to challenge the ideological foundations of neoliberalism as a model of social and economic governance. It is recognised that no social change can take place without shaking the economic ideology and the politics underpinning such ideology. Neoliberalism has been portrayed as ‘the ascendancy of financial capital over industrial capital in the pursuit of profit’.<sup>208</sup> It has suffered generalised recessions (1974-5 and 1980-82) with high unemployment, a collapse in investment, and high inflation, which has led to a long-term decline in profitability.<sup>209</sup> As has previously been explained, because of the lost battle over the achievement of Keynesian ‘full employment’, this idealistic goal<sup>210</sup> has had to surrender to more conservative and rather austere monetary policies to combat inflation. The lost battle also influenced policy makers to re-configure their focus on labour rigidities, market imperfections and distortions and, therefore, to call for competition as ‘a mechanism by which workers and units of capital are compelled to act’.<sup>211</sup> As O’Connor suggested, ‘coercive’ competition replaced the ‘socialisation’ of economic activity by embedding at its foundation ideas of state rationalisation, market contestability and mobility. It is even more interesting to uncover how these three ingredients were implemented. Contestability of markets called for the prohibition of discrimination and eradication of market barriers to ensure a level playing field which would, in turn, guarantee labour mobility so as to enable capital to be relocated profitably elsewhere and to facilitate workers’ wage flexibility (low or cheaper labour).<sup>212</sup> In contrast, the Keynesian idealistic vision was doomed to fail since it stands out for higher wages and extensive social protection.<sup>213</sup> O’Connor uncovers the fact that neoliberalism re-established unemployment in the early 1980s so as to curb welfare benefits and collective bargaining agreements which was followed by the complete liberalisation of capital markets.<sup>214</sup> Capital mobility is also said to constrain governments to pay ‘the going world rate’ to finance their fiscal deficits, to increase the bargaining power of capital owners, and to put upward pressure on the exchange rate and domestic taxation since governments must adjust to foreign tax policy requirements.<sup>215</sup> Ultimately, due to fierce competition among capital owners, ‘financialization’ pushes down credit rates and risk premiums.<sup>216</sup> Others argued that financialization contributed to a sluggish overall performance based on consumption and export-oriented growth models.<sup>217</sup>

Thus, it comes as no great surprise that the re-configuration of influence, as is envisaged by neoliberalism, has essentially led to a weakening of the social and economic position of labour. Perhaps, one of the most pervasive and destructive drivers of this ‘new’ capitalism lies primarily in its ambition to achieve the financialization of the emerging global order, much of which has actually happened. This architectural configuration seems even more plausible since the idea of economic integration has been the fundamental principle of an internal market: where individuals’ migration is achieved through free movement, and mobility has served this purpose as a cheaper source of labour which boosts capital profits through workers’ flexibility; the free movement of capital has achieved financialization and the free movement of goods has succeeded in opening up markets through active competition.

Under Article 119 TFEU, the idea of ‘free competition’ disguises the neoliberal idea of ‘coercive competition’ rather than of ‘ordered freedom’ since its macroeconomic foundations, which endorse explicitly an efficient use of

<sup>207</sup> W Röpke, *Crisis and Cycles* (London, W Hodge, 1936) 160.

<sup>208</sup> G Duménil and D Lévy, *Capital Resurgent: Roots of the Neoliberal Revolution* (Harvard University Press, Cambridge, 2004).

<sup>209</sup> See the excellent article by J O’Connor, ‘Marxism and the Three Movements of Neoliberalism’ 36 *Critical Sociology* 5 (2010) 694.

<sup>210</sup> See e.g. HM Oliver, ‘German Neoliberalism’, 74 *Quarterly J of Economics* 1 (1960) 128 on the use of Keynesian measures to combat unemployment regarded as ‘foolish’ by German neoliberals.

<sup>211</sup> *Ibid* 695.

<sup>212</sup> *Ibid* 696.

<sup>213</sup> *Ibid* 697; J O’Connor, *From Welfare Rights to Welfare Fights: Neoliberalism and the Retrenchment of Social Provision* (Mimeo, Univ of Massachusetts, Amherst, 2002).

<sup>214</sup> OECD, ‘Open Markets Matter’ (Paris, 1998).

<sup>215</sup> P Genschel, ‘Globalization and the welfare state: a retrospective’ 11 *J of European Public Policy* 4 (2004) 619, 623.

<sup>216</sup> *Ibid*.

<sup>217</sup> See E Stockhammer, ‘Financialization’ in *Handbook* (2012) 124.

Union resources by its Member States, bear much of the neoliberal austerity imprint in the convergence criteria rather than the 'human' ordoliberal ideology previously formulated. This is also revealed by another position supported by German neoliberalism<sup>218</sup> which argued that monetary policy should 'complement' monopoly policy to maintain the rule of law established by the ordoliberal concept of 'ordered' constitutional freedom. Thus, on the one hand, at a microeconomic level, this 'order' will safeguard individual economic rights, such as free enterprise or the freedom of contract, except when this promotes monopolies and, on the other hand, at a macroeconomic level, the rule of law will safeguard price stability, output, the distribution of income and the allocation of resources. Since the breakdown of Bretton Woods, the 'macroeconomics trilemma'<sup>219</sup> of open markets with free competition has favoured floating exchange rates without capital control to the detriment of other objectives of monetary policy.<sup>220</sup>

While the architectural representations of coercive freedom have not been entirely in the negative in terms of achieved impact on the economy and society as a whole - for example, one cannot deny certain positive benefits of free movement of EU citizens<sup>221</sup> - the Achilles heel of the above freedoms is currently *financialization* being used as a means to misappropriate the human capital to uncover corporate responsibility for speculative pursuits.<sup>222</sup> The social costs of this full-blown financial crisis have shown that the speculative gains of this kind have not been short-termism.<sup>223</sup> Rather, those in pursuit of speculation of profits have embraced in the long run the mature cost of a financial servicing industry which was even highly respected as a successful driver of capitalism until its 'Big Fail' finally spread across the globe.

In conclusion, the 'remaking' of capitalism would not have been possible without deregulation and competitive pressure.<sup>224</sup> As government spending was assumed to be inflationary, spending has remained static,<sup>225</sup> whereas taxation has served to increase reliance on consumption taxes, such as VAT and payroll taxes and to diminish corporate tax.<sup>226</sup>

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<sup>218</sup> Oliver 144.

<sup>219</sup> Attributed to P Krugman, 'The return of depression economics' 78 *Foreign Affairs* 1 (1999) 56.

<sup>220</sup> G Cozzi, 'Capital controls' in *Handbook* (2012) 27.

<sup>221</sup> On the other hand, O'Connor, 704, reminds us that 'even elite migrant workers are more likely to sell their labour power at a lower price and work in poor conditions', much of which is experienced in real life. Generally on fundamental freedoms see C Barnard, *The Substantive Law of the EU: The Four Freedoms* (Oxford, OUP, 3<sup>rd</sup> edn, 2010).

<sup>222</sup> Before the breakdown of Bretton Woods in 1971 it is said that only 10% of foreign exchange transactions were purely speculative.

<sup>223</sup> See also O'Connor 702.

<sup>224</sup> For example, in order to penetrate markets, administrative barriers had to fall, while not every sector of the economy could have been regulated anyway.

<sup>225</sup> Karl Otto Pohl, former president of the German Bundesbank once said: 'Inflation is like toothpaste. Once it is out of the tube, it is hard to get it back again'. Hyperinflation happened in Germany after the World War I when prices rose 10% an hour see Slavin 240.

<sup>226</sup> Ibid 709; OECD 1998, *Economic Outlook*, Paris, June 1998 which shows how corporate tax rate fell by 10.3% compared to 12.4% which corresponds to the fall of the average top marginal income.